ORIGINAL

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended;	)	CC Docket No. 96-149
	)	
and	)	
	)	
Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area	)	

COMMENTS OF AT&T CORP. ON ISSUES RELATING TO THE PROVISION OF IN-REGION INTERLATA SERVICES BY INDEPENDENT LECS

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Summary

The Commission's inquiries concerning the proper regulatory treatment of independent LECs are timely. Although independent LECs have long had the authority to provide long-distance services, SNET and other independent carriers have only recently been exploiting their local monopolies to obtain unfair and illicit advantages in providing such services. This proceeding thus provides the Commission with the opportunity to modify its existing regulations in this area in order to respond effectively to current marketplace realities.

In many respects, independent LECs do not pose as great a threat to interexchange competition as the BOCs. They tend to serve smaller and less densely populated areas, and competing interexchange carriers often interconnect with them only indirectly. At the same time, however, independent LECs are permitted to provide interexchange service today, with their bottleneck monopolies fully intact, and without first having to satisfy any of the pro-competitive preconditions required of the BOCs under Section 271.

Those monopolies are a potent source of market power, and independent LECs have both the ability and the strong incentive to abuse them to impede interexchange competition through acts of discrimination, cost misallocations, and price squeezes. At a minimum, therefore, for so long as they retain market power, independent LECs providing in-region interLATA services should be subject to the same regulatory requirements that will apply to the BOCs if and when the BOCs are permitted to provide such services --

including strict structural separation and non-discrimination requirements, advance tariff review and cost support requirements, equal access requirements, and meaningful reporting requirements. To the extent the Commission is concerned about the burden of these regulations on the smaller independent LECs, it would not be unreasonable to apply them, at least as an initial matter, solely to Tier I LECs -- all of whom are fully capable of complying with such rules, and all of whom have the potential to cause substantial competitive harm.

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COMMENTS OF AT&T CORP. ON ISSUES RELATING TO THE PROVISION OF IN-REGION INTERLATA SERVICES BY INDEPENDENT LECS

Pursuant to the Notice of Proposed Rulemaking released July 18, 1996 ("NPRM"), and the Commission's August 9, 1996 Order, AT&T submits these comments on the regulations that should apply to the provision of in-region interLATA services by independent local exchange carriers ("independent LECs").

This issue is a timely one. Although independent LECs have long had the authority to provide long-distance services, SNET and other independent carriers have only recently been exploiting their local monopolies to obtain unfair and illicit advantages in providing such services, and it is a matter of great importance to modify the existing regulations to address current marketplace realities. These Comments thus respond to those portions of the NPRM (¶¶ 108-129, 153-162) in which the Commission asks the parties to address (1) the appropriate market definitions to be used in assessing the market power of independent LECs, (2) the ability of independent LECs to abuse their market power to impede competition

in the provision of interexchange services, and (3) the regulations that should be applied to the provision of in-region interLATA services by independent LECs in light of that market power.[1]

The NPRM also seeks comment on these same issues as they apply to BOC affiliates that may in the future receive the Commission's approval to provide in-region interLATA services. AT&T's comments addressing the appropriate regulatory treatment of BOCs have been filed separately.[2] In that regard, while the BOCs and independent LECs are in some respects treated differently under the Communications Act, those differences neither require nor would justify the adoption of more relaxed regulation of the independent LECs than of the BOCs with respect to the matters raised in this NPRM. Under the Act, a BOC may be permitted to provide long-distance services only after it becomes subject to facilities-based competition in the State for which it applies, takes specified steps to open its local markets to competition, demonstrates that it will comply with the structural separation and non-discrimination requirements of Section 272, and shows that its provision of in-region interLATA services would be in the public interest. Independent LECs, by contrast, may provide such services

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[1] The Commission's Notice of Proposed Rulemaking initially set an August 15, 1996 deadline for the submission of comments on all issues raised in the NPRM. The Commission subsequently established a separate pleading cycle, with comments due August 29, 1996, solely with respect to the issues raised in the NPRM relating to the proper regulatory treatment of independent LECs, while maintaining the August 15, 1996 deadline with respect to all other issues. See Order, DA 96-1281 (released Aug. 9, 1996).

[2] See Comments of AT&T Corp. (filed Aug. 15, 1996) ("AT&T's August 15 Comments").

today -- before their bottleneck monopolies have eroded in any respect. At a minimum, therefore, for so long as they retain market power, independent LECs providing in-region interLATA services should be subject to the same regulatory requirements that will apply to the BOCs if and when the BOCs are permitted to provide such services.

I. The Commission Is Correct That Its Competitive Analysis Must Focus On Calls Originating In The LEC's Service Area.

As a threshold matter, the NPRM requests comment (¶¶ 115-129) on how it should apply in this proceeding the market definition approaches proposed in the Interexchange NPRM[3] if such approaches are ultimately adopted and, if the Commission does not adopt those approaches, how the relevant product and geographic markets should instead be defined for this proceeding. AT&T set forth its position on the proposed market definition approaches at length in its comments in response to the Interexchange NPRM, and incorporates these comments here by reference.[4]

As AT&T has previously shown, the interexchange market definition is irrelevant to the issue of whether the LECs could

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[3] See Notice of Proposed Rulemaking, Policy and Rules Concerning the Interstate, Interexchange Marketplace; Implementation of Section 254(g) of the Communications Act of 1934, CC Docket No. 96-61, (released Mar. 25, 1996) ("Interexchange NPRM").

[4] See AT&T Comments on Market Definition, Separations, Rate Averaging and Rate Integration, pp. 2-28, Policy and Rules Concerning the Interstate, Interexchange Marketplace; Implementation of Section 254(g) of the Communications Act of 1934 (filed April 19, 1996) ("AT&T Interexchange Comments"); Reply Comments of AT&T Corp. on Market Definition, Separations, Rate Averaging and Rate Integration, pp. 2-9, Policy and Rules Concerning the Interstate, Interexchange Marketplace; Implementation of Section 254(g) of the Communications Act of 1934 (filed May 3, 1996).

abuse their power in the local market to impede interexchange competition. Settled law establishes that market definitions and market share analyses are unnecessary when the presence of market power can be proven directly -- as it can here, because of the LECs' control of local bottleneck facilities that are essential to the provision of long-distance service -- or when undisputed power in one market (local services) can be leveraged to impede competition in a second market (interexchange). The proper markets to analyze here, therefore, are the markets for local and access services -- the markets where those bottlenecks exist -- rather than the interexchange market.[5] In this regard, while interexchange services originating in a particular LEC's service area generally could not be a separate geographic market,[6] the Commission is nonetheless correct insofar as it concludes (¶ 126) that a determination of the appropriate regulatory treatment of a LEC's in-region interLATA services should focus on these areas.

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[5] See AT&T Interexchange Comments, pp. 2-14.

[6] As AT&T explained in its Interexchange Comments (pp. 14-23), the Commission's existing market definition is correct in other contexts -- i.e., determining the appropriate regulatory treatment of interexchange carriers that possess no bottleneck power. Moreover, the Commission has properly defined the interexchange market as a single national market because even though there is not perfect demand substitution for interexchange services originating in different regions, there will be perfect supply substitution so long as each LEC will allow any carrier to offer interexchange services to the LEC's customers on nondiscriminatory terms. For example, while a caller that wishes to place a call between two cities will not regard calls between other cities as substitutes (see NPRM, ¶ 123), every market participant has the ability to provide services in every area of the country. Under those circumstances, the Commission's existing "single national market" definition is the only approach that is consistent with settled legal and economic principles, including the Justice Department's Merger Guidelines.

Indeed, that is precisely the approach the Commission has adopted in classifying U.S. international carriers as dominant or non-dominant. Pursuant to the Commission's rules, a U.S. carrier that is affiliated with a monopoly foreign carrier is presumptively classified as dominant for calls along the route between that country and the United States.[7] A U.S. carrier that seeks to be classified as non-dominant but is affiliated with a non-monopoly foreign carrier still bears the burden of showing that its affiliate "lacks the ability to discriminate . . . through control of bottleneck services or facilities."[8] In such instances, the inquiry is properly focused on "the scope or degree of the foreign affiliate's bottleneck control" in the market in which that control exists.[9] These regulations recognize, as does the NPRM, that affiliation with a carrier that controls bottleneck facilities is a significant source of market power, and that determining the proper regulatory classification of an entity with such an affiliation requires careful scrutiny of the market in which the affiliated carrier has its bottleneck.

II. LECs' Monopoly Control Over Essential Facilities In Their Local Markets Enables Them To Exercise Market Power In The Interexchange Market.

There is no dispute that the BOCs can use monopoly control over bottleneck local facilities to impede competition in interexchange services. As the NPRM explains, the BOCs can

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[7] See 47 C.F.R. § 63.10(a)(2).

[8] See 47 C.F.R. § 63.10(a)(3).

[9] See id.

potentially leverage this monopoly power into interexchange services by raising their rivals' costs through acts of discrimination, cost misallocation, the charging of excessive prices for access, and similar abuses (¶¶ 130-141).[10] The same is true of independent LECs, for they likewise have monopoly control over facilities and services upon which their interexchange competitors are critically dependent.[11]

Moreover, unlike the BOCs, independent LECs may provide interexchange service right now. Section 271 prohibits any BOC from providing in-region interLATA services today, and provides that a BOC will not be permitted to provide such services in the

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[10] The Commission recognizes (¶ 139) that the BOCs could discriminate against interexchange competitors in numerous and subtle ways that would be exceedingly "difficult to police, particularly in situations where the level of the BOC's 'cooperation' with unaffiliated interLATA carriers is difficult to quantify." In contrast, however, it suggests (¶¶ 135, 137) that cost misallocations would impair competition only in the event that they enabled the BOC to drive other interexchange carriers out of the market and then raise prices to supracompetitive levels. As AT&T showed in its August 15 Comments (pp. 63-64), cost misallocations need not produce such an extreme result in order to have a seriously anticompetitive effect. To the contrary, by raising the costs for competitors' services, cost shifting would harm competition and consumers by forcing competitors to charge higher prices for their services, and by diverting customers from those competitors to the BOC affiliate regardless of the affiliate's comparative efficiency.

[11] This is not to say that the BOCs generally do not pose a greater threat to competition. The bottleneck facilities of independent LECs extend over smaller geographic areas than those of the BOCs (see NPRM, ¶ 147), they generally serve less densely populated areas, and interexchange carriers often interconnect to independent LEC exchanges only indirectly (i.e., through a BOC). Moreover, it is far less likely that an independent LEC will be providing access at both the originating and the terminating ends of a call than that a BOC will control both ends. At the same time, some of the independent LECs, such as SNET and GTE, serve areas that are of substantial size by any measure.

future unless it meets its burden of showing that there is facilities-based competition in its relevant local markets, that it has fully implemented a 14-point checklist designed to foster additional local competition, and that its entry would serve the public interest -- at which point it will then be subject to the full range of structural separation and non-discrimination requirements of Section 272. The independent LECs, in contrast, are permitted today to provide interexchange service with their local monopolies fully intact and, at least under current regulations, on a predominantly integrated basis without the safeguards established by Section 272. At present, therefore, the opportunities for independent LECs to abuse their considerable market power are for the most part unconstrained.[12]

III. The Commission Should Adopt Appropriate Regulations To Check The Potential Abuse Of Market Power By Independent LECs.

The Commission's current rules are patently inadequate to address the potential abuse of market power by independent LECs. Under those rules, an independent LEC may either provide interexchange services directly (in which case it is classified as dominant), or through an affiliate that (1) maintains separate books of account, (2) does not own jointly with the LEC any transmission or switching facilities, and (3) obtains exchange

[12] Moreover, although the Act treats BOCs and independent LECs differently in many respects, there is at least one critical respect in which they are treated the same: both are subject to the requirements of Section 251. However, while Section 271 may provide the BOCs with some incentive to adhere to the requirements of Section 251 and the interconnection regulations adopted by the Commission, the independent LECs, who can provide long-distance service today, have no comparable incentive.

services at tariffed rates and conditions (in which case it is classified as non-dominant).[13] They thus permit an independent LEC to choose between complying with very modest separation requirements and no separation requirements, and to be classified as non-dominant or dominant on the basis of that choice.

These rules are seriously flawed in at least three respects. First, independent LECs should not be permitted to choose between few separation requirements and no separation requirements. Under either regime, the LECs are permitted to engage in joint and integrated design, planning, and provisioning of exchange and interexchange services. This integration both inherently discriminates against other carriers, and permits the costs of long distance operations to be misallocated to monopoly services and ratepayers with practical impunity, thereby both cross-subsidizing long distance services and raising the LECs' rivals' costs.[14] There is no sound policy reason to permit such competitive harms when they are caused by independent LECs with current absolute monopolies, but prohibit them when they are caused by BOCs who, by contrast, at least have satisfied Section 271. The Commission should therefore impose the same strict structural

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[13] See Fifth Report and Order, Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorizations Therefor, 98 F.C.C.2d 1191, 1198 (1984).

[14] See AT&T's August 15 Comments, pp. 16, 18.

separation and non-discrimination requirements on both classes of carriers.[15]

Second, the separation requirements should be imposed in conjunction with, not as a substitute for, the other regulations that are necessary to safeguard against the risk of anticompetitive conduct. Specifically, in addition to the separation requirements, advance tariff review and cost support requirements should be imposed in order to discourage predation and price squeezes and make such conduct more detectible, and reporting requirements should be established to discourage discriminatory conduct and enforce the rules that prohibit it.[16]

Third, the Commission should make clear that equal access requirements apply with full force to independent LECs -- including the requirement that a customer seeking local service from such carriers be presented with his or her options for interexchange service in a neutral fashion. Thus, when customers call to order

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[15] AT&T has previously addressed in detail the appropriate content of those requirements, and incorporates that discussion here by reference. See id., pp. 16-47.

[16] See id., pp. 36-38, 66. As AT&T has previously stated (id., pp. 65-66), some aspects of dominant carrier regulation, such as stringent Section 214 requirements and price ceilings, do not address the leveraging concerns presented by LEC provision of interexchange services, and it therefore may not be necessary to apply the full panoply of dominant carrier regulation in this context. Indeed, because dominant carrier regulation was not designed to address the precise risks presented by monopoly leveraging, it is particularly incongruous that the current rules permit independent LECs to avoid even the modest separation requirements of Competitive Carrier if they are willing to accept a classification as dominant. Conversely, some aspects of dominant carrier regulation -- such as advance tariff review, price floors, and cost support requirements -- do address such concerns, and should be imposed in conjunction with the other regulations discussed herein.

local service, or when existing local customers contact a LEC to advise it that they are switching primary interexchange carriers ("PICs"), such contacts should not be converted into marketing opportunities to persuade the customer to choose the LEC's interexchange service and dissuade it from choosing another carrier's. Such conduct is a clear abuse of the independent LEC's market power.

The need to reaffirm the applicability of these rules is sharply underscored by the present conduct of SNET, which has repeatedly abused its position as the incumbent local exchange carrier for Connecticut. For example, SNET has instituted and actively marketed to its own long distance customers a "PIC-freeze" which requires the subscriber to contact it directly when he or she wishes to switch long-distance carriers, rather than permitting the long-distance carrier the customer chooses to advise SNET of the switch. However, SNET has refused to honor identically-worded PIC freeze requests submitted to it by AT&T's long distance customers. AT&T has also received numerous reports that when customers contact SNET to establish local service and presubscribe to a long distance carrier, the SNET representatives either extol the purported benefits of SNET's long distance service and omit any mention that AT&T is an available carrier choice or, if the customers indicate a preference for AT&T as their long distance carrier, urge the customers to reconsider and proceed to market its own service on

the same call.[17] The Commission should reaffirm that such abusive practices are impermissible.

AT&T agrees with the Commission (¶ 153) that only those independent incumbent LECs that control local exchange or exchange access facilities should be subject to the requirements adopted in this proceeding, and that the Commission should rely on the definition of "incumbent local exchange carrier" provided in 47 U.S.C. § 251(h). Carriers that do not possess market power over local exchange services do not present any risk of anticompetitive leveraging, and application of these regulatory requirement to such LECs would therefore be unwarranted.[18]

Moreover, to the extent the Commission is concerned about the burden of these regulations on the smaller independent LECs, it would not be unreasonable to apply them, at least as an initial matter, solely to Tier I LECs. See NPRM, ¶ 159. The Commission could reasonably conclude that the costs of imposing these requirements (with the exception of the equal access requirements) on small carriers outweigh the likely benefits, given the scope of the smaller carriers' operation and the more limited competitive harm they could inflict. Conversely, larger LECs, such as SNET and

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[17] Conversely, when a customer calls SNET and seeks to change long-distance carriers from AT&T to SNET, SNET simply makes the change.

[18] AT&T also agrees with the Commission (¶ 160) that the same rules should apply both to an independent LEC's provision of in-region domestic interexchange service and to its provision of in-region international interexchange services. The competitive risks in each case are the same.

GTE, plainly are fully capable of complying with such rules, and have the potential to cause substantial competitive harm.

Respectfully submitted,

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